CHARITABLE GIVING

CONSIDERATIONS FOR VENTURE CAPITALISTS

Many successful entrepreneurs and investors use their time and personal wealth to support charitable causes. In addition to helping those in need, charitable giving can serve as a means to achieve your long-term financial goals. For example, gifting interests in privately held companies is an increasingly common tax and estate planning strategy. Charitable gifting can also be a viable way for venture capital fund managers to rebalance their personal portfolios.

"Gifting complex assets through a DAF can provide the donor with significant tax benefits."

For VCs seeking to balance their portfolios, donating an interest in a portfolio company may be a practical alternative to selling, particularly because a sale may indicate a lack of confidence in the investment. Gifting can allow VCs to reduce their exposure to a particular industry or stage of development without sending negative signals to the market. Furthermore, donations also carry tax benefits and allow VCs to support charitable causes that are aligned with the values of their remaining holdings.

An optimal method for donating a VC interest is to establish a donor-advised fund (DAF). Below we discuss DAFs in more detail and explain the benefits they can provide to donors of VC investments.

What is a Donor-Advised Fund?

A DAF is a charitable giving vehicle that is administered by a growing number of public charities. Some of the nation's largest sponsors of DAF programs are Fidelity Charitable, Schwab Charitable, Vanguard Charitable, and National Christian Foundation.

DAF programs function by accepting irrevocable contributions of assets and placing them in an account where they are invested and grown tax-free. In many cases, the donor is allowed some degree of control over how their contributions are allocated, typically among a set of pre-defined investment options. Donors then make grant recommendations from their DAFs to specific charities, which are generally subject to due diligence by the sponsor to ensure funds are used for charitable purposes. DAF sponsors generally accept donations of a variety of different asset types, including cash, publicly traded securities, personal property, real estate, and life insurance policies.

Complex Assets

Many of the national DAF program sponsors and large community foundations have started accepting gifts of complex assets. Over the past two years, Fidelity Charitable, the sponsor of the nation's largest DAF program, has received a total of nearly $1 billion in donations of complex assets, the vast majority of which are highly appreciated non-publicly traded assets like private equity and VC investments.[1]

It's important to note that smaller organizations with DAF programs may not be capable of accepting gifts of VC interests and other complex assets because they lack the resources or infrastructure to generate liquidity from them. However, there are many well-known DAF providers that are willing and able to hold VC or private equity investments until a scheduled or planned exit date, allowing the full value of the investment to be realized and the proceeds to be placed in a DAF account tax-free.

Benefits of Gifting

Gifting complex assets through a DAF can provide the donor with significant tax benefits. Upon gifting a non-publicly traded security to a DAF, the donor becomes immediately eligible for a tax deduction equal to the fair market value of the asset if it has been held for more than a year. The donor would also eliminate any capital gains tax liability when the interest is liquidated. For gifts of highly appreciated assets like most VC and private equity investments, the tax savings can be substantial.

For philanthropically minded investors, this gifting strategy is ideal because it increases the overall value of the donation. If a VC investor sold his interest, then donated the proceeds directly to a charity, he would be eligible for a tax deduction, but would be forced to pay capital gains tax on the sale, reducing the overall dollar amount of the donation.

Taking Action

VC investors considering gifting as an exit strategy should first consult their legal and tax advisors to weigh their best options. Additionally, if the DAF program you select provides a variety of investment options, you may also consider working with your financial advisor to develop a long-term gifting strategy.

[1] http://www.wsj.com/articles/more-clients-gifting-private-stock-via-donor-advised-funds-1403010401

It's also important to note that when gifting an interest in a privately held company, you will likely be required to obtain a business valuation to satisfy tax reporting requirements. According to the IRS, if the value of the gift exceeds $10,000, you are required to obtain a valuation from a qualified appraiser in order to claim a tax deduction.

In summary, donating an interest in a VC investment is an alternative gifting strategy that can help you not only meet your philanthropic goals, but also help you balance your portfolio. Gifting through a donor-advised fund can help you establish a sustainable gifting strategy, allowing you to support causes that are either personally important, or charities whose work is aligned with your company's values, over an extended period of time. Additionally it can provide significant tax benefits, which ultimately increases the overall value of your contribution.